

# Modernizing Social Security: Caregiver credits

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Chestnut Hill, Mass.: Center for Retirement Research at Boston College, August 2018

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# MODERNIZING SOCIAL SECURITY: CAREGIVER CREDITS

BY ALICIA H. MUNNELL AND ANDREW D. ESCHTRUTH\*

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## Introduction

Women still tend to work fewer years and earn less than men, which leads to less income in retirement. One reason is that women are often still the main family caregiver. Traditionally, Social Security has recognized this role by providing spousal and widow benefits for married women. Today, however, many women are not eligible for these benefits because they never married or they divorced prior to the 10-year threshold needed to qualify. Even those who are married are less likely to receive a spousal benefit, as their worker benefit is larger. Thus, many mothers receive little to no support to offset lost earnings due to childrearing.

Given this concern, some policy experts propose wage credits to boost a caregiver's earnings record and, thus, her retirement benefits. Such credits – which sometimes cover caring for an elderly relative as well as a child – are common in other developed countries. These credits are designed to serve one or more goals, which may include improving benefit adequacy, rewarding unpaid care, or even encouraging new parents to return to work. For the United States, being clear about the credits' objective is important in assessing what program design offers the best fit.

This *brief* is the second in a series on modernizing Social Security to account for changing social, economic, and demographic circumstances.<sup>1</sup> The discussion proceeds as follows. The first section describes Social Security benefits and changing family patterns. The second section looks at caregiver benefits in two other countries. The third section covers U.S. reform proposals, while the fourth assesses these proposals based on three criteria: targeting efficiency, administrative feasibility, and cost offsets. The final section concludes that support for caregiving can be well targeted if the goal is clear; administering a credit is relatively easy; and the cost could be offset by reducing benefits somewhat for higher earners.

## Social Security and Changing Family Patterns

Social Security was designed in the 1930s when, typically, the husband was the breadwinner and the wife a homemaker. The program included spousal and widow benefits designed for this standard one-earner household. Although these family benefits are not

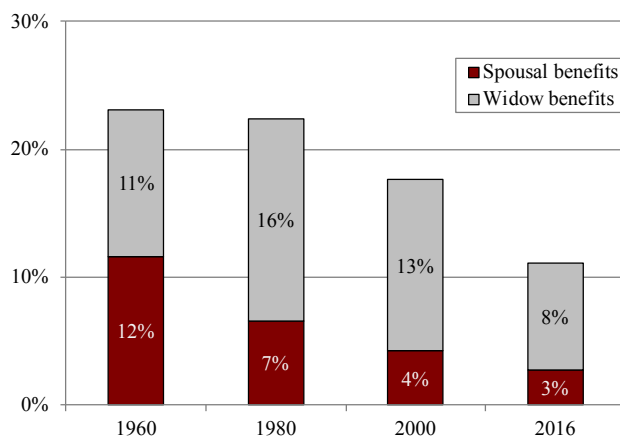
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gender based, they typically go to women because women generally work fewer years and earn less than men.

The ability of women to receive family benefits has declined sharply in recent decades as their employment patterns and the nature of the family unit have changed dramatically. On the employment front, the labor force activity of married women has shot up, which means that they increasingly receive benefits based on their own earnings record and are much less likely to receive spousal or widow benefits (see Figure 1).

FIGURE 1. SPOUSAL AND WIDOW BENEFITS AS A PERCENTAGE OF TOTAL BENEFITS FOR RETIRED WORKERS, SPOUSES, AND WIDOWS, 1960-2016

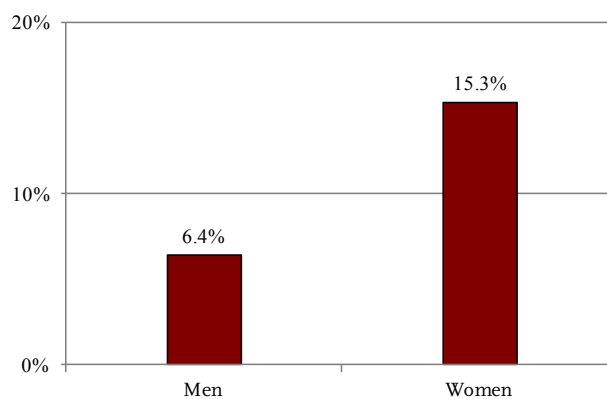


Source: Authors' calculations from U.S. Social Security Administration (2018).

Despite their increased workforce activity, women continue to be at a disadvantage in the labor market compared to men. Research suggests that part of the reason is caregiving duties, which can reduce work hours and affect access to better-paying jobs.<sup>2</sup> For example, women ages 25-44 – those most likely to have young children – work part time more often than men (see Figure 2). Even when working full time, women earn only about 80 percent as much as men.<sup>3</sup>

At the same time, fewer women are eligible for Social Security family benefits due to divorce and marriage patterns. The increasing divorce rate has resulted in about 25 percent of first marriages ending

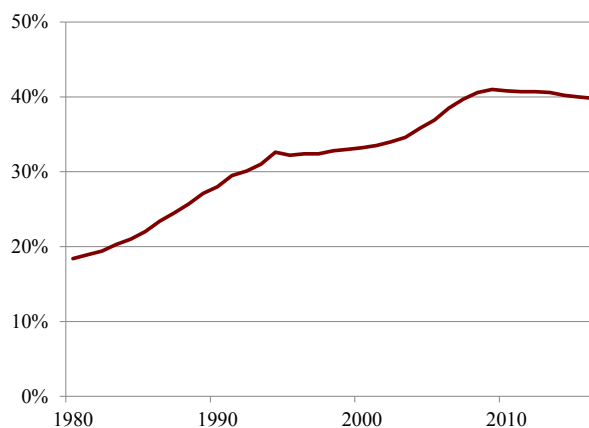
FIGURE 2. PERCENTAGE OF WORKERS EMPLOYED PART-TIME BY GENDER, AGES 25-44, 2016



Source: U.S. Census Bureau, Current Population Survey (CPS) (2017).

within 10 years, the eligibility threshold needed for access to family benefits.<sup>4</sup> And childbearing among unmarried women has increased sharply – from 18 percent of all births in 1980 to 40 percent today (see Figure 3).

FIGURE 3. PERCENTAGE OF BIRTHS TO UNMARRIED WOMEN, 1980-2016

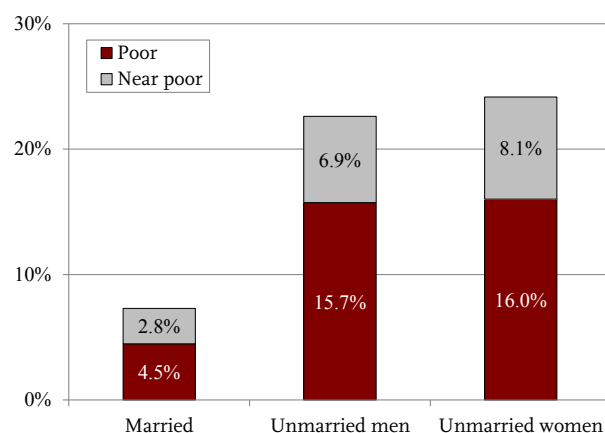


Sources: Organisation for Economic Co-operation and Development (2018); and Centers for Disease Control and Prevention (2018).

These trends have sharply increased the percentage of households headed by single mothers, leaving a wide swath of women with no access to family benefits. In addition, compared with married mothers, single mothers face more labor market constraints from their childcare responsibilities, impeding their job prospects and reducing their ability to earn an adequate Social Security benefit.

Overall, the changes in labor market and marital patterns mean that large numbers of women are going to move through retirement with more disadvantages than their earlier counterparts. Not surprisingly, among those ages 65 and over, poverty rates for unmarried women exceed those of unmarried men (see Figure 4). And unmarried women account for

FIGURE 4. PERCENTAGE OF INDIVIDUALS AGES 65+ WHO ARE POOR AND NEAR POOR BY MARITAL STATUS, 2016

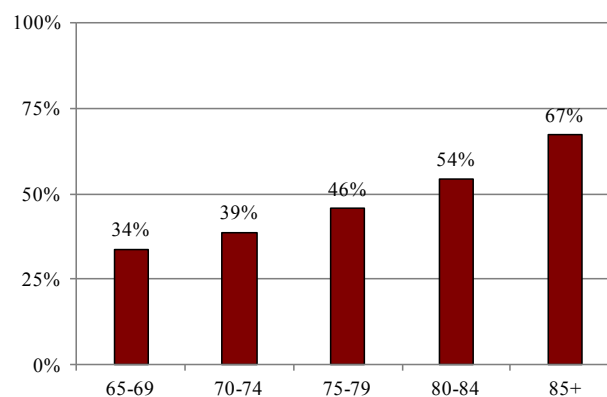


Source: Authors' calculations from 2017 CPS.

one-third of all households ages 65-69 and two-thirds of households ages 85 and over (see Figure 5). Childcare responsibilities are a major contributor to low income in retirement. One study found that women ages 65-74 who spent at least 10 years as a single mother were 55 percent more likely to be poor than continuously married mothers of similar education and ethnicity.<sup>5</sup>

Because of the poor outlook for retirement income among single women and a growing sense that the economic value of caregiving should be recognized, many policy experts have advocated caregiver credits.<sup>6</sup> Such credits are a near universal component of public pension systems in other higher-income countries.

FIGURE 5. UNMARRIED WOMEN AS A PERCENTAGE OF ALL HOUSEHOLDS, AGES 65+, 2016



Source: Authors' calculations from 2017 CPS.

## Caregiver Credits in Other Countries

While caregiver credits are common in developed countries, the form of these credits varies, in large part because the objectives vary.<sup>7</sup> The primary objective is to improve retirement benefit adequacy for women, but countries also use credits to promote higher fertility rates, to encourage new mothers to return to the labor force by offering a bonus to working caregivers, or simply to reward the provision of unpaid care. One commonality among these programs is that they link credits to parenthood, not marital status. For examples of caregiver programs, this section looks at the United Kingdom, Sweden, and Germany.

Designing a childcare credit involves addressing several issues: 1) the number of years an individual will be eligible to receive credits; 2) how credits will be calculated; 3) who is eligible to receive credits (i.e., a mother, a father, or both); and 4) whether an individual has to be out of the labor force completely to receive the credit. The countries discussed below have made different decisions that reflect differing objectives. The United Kingdom and Germany are among the few countries that offer credits for taking care of elderly or sick relatives as well as children.

### *Child and Adult Care Credits in the U.K.*

The state pension system in the United Kingdom has two components: a Basic State Pension (BSP) and an Additional State Pension (ASP). Individuals qualify for these pensions by making National Insurance Contributions (NIC) based on their earnings or by serving as a caregiver. A parent who is caring for children under the age of 12 and earns too little to make NIC contributions can receive qualifying years towards the BSP. To receive the maximum BSP benefit, individuals need a total of 35 years. During 2002-2016, parents were also eligible for accruing earnings credits towards the ASP equal to the program's lower earnings limit. In both cases, to be eligible, parents need(ed) to be registered for the Child Benefit, a cash payment available to parents with children under 16. Parents can also earn pension credits while on parental leave after the birth or adoption of a child.

The United Kingdom offers similar pension credits to those who receive a Carer's Allowance for providing care to a disabled child or adult for at least 35 hours per week. This program is means-tested and the person under care must be receiving government benefits that fall under a disability designation.<sup>8</sup>

### *Childcare Credits in Sweden*

The Swedish public pension system offers credits for caregiving to parents with children up to age four. The parent with the lowest earnings in the year prior to childbirth gets the credit. No limit is placed on the number of years for which a parent can receive the credits. However, retirement benefits cannot be based solely on credits; work history is also required.

The credits are calculated in three different ways, with each method targeted to a specific type of caregiver. A caregiver receives the highest of the three amounts. Under the first calculation, the credit is equal to a person's earnings in the year before the birth. This method helps workers who had relatively high earnings prior to childbirth and significantly reduced their work hours afterwards. Under the second calculation, the credit is equal to 75 percent of the average earnings in Sweden in the year before childbirth, which helps those who had relatively low earnings prior to childbirth and then reduced work hours

significantly. Under the third calculation, workers get a bonus if they work about the same hours as before childbirth, which ensures they are not disadvantaged relative to those who sharply cut back their hours.

### *Child and Adult Care Credits in Germany*

In Germany, the parent who is mostly responsible for childcare receives annual pension credits for the first three years of the child's life. The amount is equal to the pension credit received by an average German earner. In addition, since a 2001 reform, Germany has offered credits up to the same amount for parents who keep working while raising a child ages three to 10. This credit provides an incentive for parents to return to work while providing childcare. The law also

offers credits to parents who leave the labor force completely to care for two or more children – if one is younger than 10.

In addition to recognizing childcare efforts, Germany provides credits for caring for elderly or sick relatives through its long-term care insurance (LTC) program. To qualify, a caregiver must work fewer than 30 hours a week and the person under care must receive benefits through the LTC program. The size of the credit depends on both the number of care hours provided per week and the level of nursing care dependency. The credits are paid by long-term care insurance and have no lifetime limit.

### *Implications for the U.S.*

The extensive experience with childcare credits in other developed countries suggests that these programs can be designed to meet specific objectives and can be administered effectively. On the other hand, the mix of designs suggests that any consideration of caregiver credits should begin by determining the primary policy objective. Finally, the fact that one of the few caregiver programs for dependent adults is linked to Germany's long-term care insurance program highlights the challenges of administering such an effort; it underscores the need for reliable data on both the care requirements of the elderly and the hours of effort provided by the caregivers. For simplicity, the following discussion is limited to childcare credits.<sup>9</sup>

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**“The design of caregiver credits varies based on a country's specific policy objectives.”**

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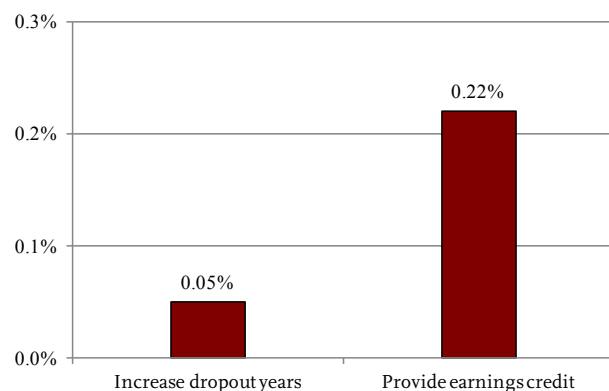
## Childcare Credits for the U.S.

U.S. policy experts have proposed two main types of childcare relief through Social Security.<sup>10</sup>

- Increase the number of work years that are *excluded* from benefit calculations. The current Social Security benefit formula is based on a worker's highest 35 years of earnings. Under this proposal, parental caregivers could drop up to five additional years from the benefit calculation, reducing it from 35 to 30. The policy would apply to those caring for children under age six. Parents must have zero earnings in a given year to qualify, and only one parent could claim it per year. Each parent could earn, at most, two "dropout years" per child, and a maximum of five dropout years in total.<sup>11</sup>
- Provide earnings credits to parents with a child under age six for up to five years. The credit for each year of care would equal one half of the Social Security Administration's (SSA) average wage index (about \$24,682 in 2016). The credits would be available for all past years to newly eligible beneficiaries starting in 2018. The five years selected for the credits would be those that produce the largest increase in a worker's career earnings.<sup>12</sup>

Increasing the dropout years in the calculation of average earnings is relatively inexpensive, while crediting one half of the SSA average wage has a more significant cost (see Figure 6).

FIGURE 6. COST OF CHILDCARE PROPOSALS AS A PERCENTAGE OF TAXABLE PAYROLL OVER 75 YEARS



Source: U.S. Social Security Administration (2017).

The effectiveness of each approach has been explored in earlier studies.<sup>13</sup> One study that examined the poverty-reducing effect of dropout years found that this policy had very little impact overall, since many women receive spousal or widow benefits rather than worker benefits. It also found that dropout years were more beneficial to women of higher socioeconomic status (SES), because they tended to work fewer years than their lower-SES counterparts.<sup>14</sup> However, this study was done nearly 25 years ago so it may not reflect today's environment. For example, as noted above, a declining percentage of women are eligible for family benefits, so more might be able to take advantage of caregiver support today.

A couple of studies found that the childcare credit proposal would have modest effects overall, but would particularly help women at the bottom of the lifetime earnings distribution.<sup>15</sup> Similarly, another study found that credits would be more effective than either current spousal benefits or dropout years at reducing poverty for low-income groups and minorities.<sup>16</sup>

## Targeting, Administration, and Offsets

To assess any proposal, it is important to consider its targeting, administrative feasibility, and financing.

### Targeting

Evaluations of caregiver credits have focused primarily on their impact on the most vulnerable, but these credits can benefit a broader income spectrum as well. Social Security is an earnings replacement program, and parental caregivers across the spectrum have lower earnings and worker benefits due to their family responsibilities. In addition, increasingly, these caregivers will not receive spousal and widow benefits. One option noted above is to replace a specified number of years of zero earnings with some dollar credit. Sweden provides different credits for high and low earners and for those who continue to work, which recognizes the importance of childrearing and compensates a caregiver for the loss of earnings.

A related question is whether policymakers want new parents to stay home or return to work quickly. Most babies benefit from having a parent around during the early months.<sup>17</sup> Staying home is often extremely difficult in the United States due to lost earnings, so caregiver credits would be one small way of reducing the long-term costs of taking time off for



parenting. On the other hand, the system should not penalize those who return to work, so following the Swedish approach of also providing credits for these individuals would recognize the dual roles that many parents play. It also acknowledges that caregiving can take a toll on the earnings of working parents, not just stay-at-home parents.

In short, it is difficult to evaluate the targeting of the existing proposals without a clear picture of the problem that policymakers are trying to solve. It seems like a more complex issue than just introducing a mechanism to raise the benefits of very low-income women.<sup>18</sup>

## Administration

While the first challenge is designing a childcare credit program, the second is administering it. The United Kingdom simply requires that parents produce the birth or adoption certificate. In Sweden, the process is essentially automatic. All of the information needed to administer the credits is in a civil registry maintained by the Swedish Tax Agency. These data are transferred to the Swedish Pensions Agency on a daily basis, along with earnings records, to determine which parent should receive the credits. In Germany, the agency administering the program is immediately notified by the registry office when a child is born. Parents who share childcare duties can also state in advance which months should be credited to each parent.

Although the administration of childcare credits has not presented any major difficulties in these countries, the challenges could be greater in the United States until the system is fully up and running. For example, children's birth records are not always linked in SSA files to their parents' records. During the start-up phase, then, some parents seeking to claim a caregiver credit would need to document a relationship to their children.<sup>19</sup> Thus, when they claim benefits, they could be required to present their children's birth certificates. As the system matures, SSA would eventually have this information for everyone when a child is born. Basically, once the system is established, administration should not be a major hurdle. (As noted above, a credit for caring for dependent adults would be more complicated to administer.)

## Cost Offsets

The final challenge is how to finance caregiver credits. Many countries pay for these credits out of general revenues. In both Sweden and Germany, the federal government finances caregiver credits for unpaid childcare through transfers to the social insurance system, although in Germany the transfer is well below the actual cost of the credits. The United Kingdom does not specifically use general revenues to pay for its caregiver credits, relying instead on payroll taxes. However, if these taxes are insufficient in any given year to cover all pension benefits, the shortfall is covered by general revenue transfers.

In the United States, childcare credits would likely be funded within the Social Security program, because it is set up to be self-financing. Given fiscal constraints, the cost should be offset by reducing other benefits. For example, one option for offsetting the costs of either caregiver proposal is to decrease benefits for higher earners by lowering the 15-percent benefit factor currently applied to earnings above \$5,397 per month (about \$65,000 per year). Reducing the 15-percent factor to 13 percent over the next five years would cover the cost of the "dropout year" option, while reducing it to 8 percent would offset the "earnings credit" option.<sup>20</sup>

## Conclusion

It is easy to understand the appeal of crediting Social Security records to reflect lost earnings due to caring for a child. In the past, this activity was usually compensated for by the spousal benefit, but changes in women's work and marriage patterns have left fewer eligible for it. A credit is also more appealing than a spousal benefit if the goal is to compensate for the costs of childrearing, independent of marital status.

Virtually every developed country has some form of childcare credit, so many options are available. The key for U.S. policymakers is to determine the primary goal of such a credit – improving the lot of mothers generally or increasing benefit adequacy for the most vulnerable. Fortunately, even if the primary goal is to help mothers generally, a credit would also help improve benefit adequacy because mothers tend to be at higher risk for poverty. Administration of the program, once up and running, appears not to pose any substantial difficulties based on the experiences of other countries. Finally, the cost could be covered by reducing benefits somewhat for higher earners.

## Endnotes

- 1 The first *brief* (Munnell and Eschtruth 2018) provided an overview of the full series.
- 2 Bertrand, Goldin, and Katz (2010) look at the impact of childcare responsibilities on young professionals. Van Houtven, Coe, and Skira (2013) examine the impact of eldercare responsibilities on spouses and adult children.
- 3 Goldin (2014) and Blau and Khan (2016).
- 4 Authors' calculations from the U.S. Census Bureau, *Survey of Income and Program Participation* (2008). For a similar analysis, see Stevenson and Wolfers (2007).
- 5 Johnson and Favreault (2004).
- 6 Aside from caregiver credits, many governments offer other child-related subsidies. For example, the United States provides both a Child Tax Credit for having children and a Child and Dependent Care Credit to help cover daycare expenses; this latter credit explicitly recognizes a market value associated with caregiving when it is provided outside of the family.
- 7 Much of the following discussion is based on Jankowski (2011) and Fultz (2011).
- 8 Sources for the information in this section include a variety of guides to pension and child benefits available on the U.K. government website: <https://www.gov.uk>.
- 9 Interestingly, one recent U.S. proposal – the “Social Security Caregiver Credit Act of 2017” (S. 1255) – would provide earnings credits for those who care for either children or adults.
- 10 A different, and narrower, idea related to helping new parents has recently gained currency among some policy experts and legislators. This policy would provide the option for parents to take paid leave after a birth or adoption for a brief period (e.g. 12 weeks) in exchange for a reduction in their Social Security benefits at retirement. See, for example, Shapiro and Biggs (2018) and Rubio (2018).
- 11 This proposal was included in a 2016 bill by former Rep. Patrick Murphy (D-FL).
- 12 See, for example, Entmacher, Waid, and Veghte (2016).
- 13 For an overview of the literature, see Favreault and Steuerle (2007).
- 14 Iams and Sandell (1994).
- 15 Favreault, Sammartino, and Steuerle (2002) and Favreault and Steuerle (2007).
- 16 Herd (2006).
- 17 See Galtry and Callister (2005) for a review of the literature.
- 18 Social Security has another feature – a minimum benefit – that, if improved, could provide a more effective floor of support for those with low earnings by itself. However, some advocate enacting a caregiver credit as part of a minimum benefit improvement to expand the number of workers eligible for a minimum benefit. A forthcoming *brief* in this series will specifically address the minimum benefit policy.
- 19 Interestingly, general documentation requirements for Social Security were minimal for several decades after the program started. For example, individuals applying for a Social Security number were not required to submit proof of identity until 1978. See Cronin (1985) for a discussion of Social Security's administrative procedures during this period.
- 20 These specific offsets are authors' calculations from the Social Security actuaries' estimates (U.S. Social Security Administration 2017).



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